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Kenya Coffee Update Report

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Approved by:

Kevin N Smith
U.S.

Prepared by:

Mary Onsongo

Report Highlights:

Kenya coffee production forecasts to reach an all time low during MY 2007/08 mainly due to a severe coffee berry disease attack. GOK has put in place reforms to resuscitate the ailing coffee industry.

Includes PSD Changes: Yes
Includes Trade Matrix: Yes
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Production

Kenya's coffee production is forecast to reach a historic low in MY 2007/08 (estimated at 40,000 tons), representing a 22 percent decline from the previous year. The decline is mainly attributed to the progression of the Coffee Berry Disease CBD) but has been exacerbated by several other factors ranging from competition from other producers (i.e. Vietnam), market glut, market liberalization problems, cooperative management inefficiencies, high costs of production, and poor husbandry practices among the smallholders. The industry has also suffered from the effects of a strong shilling and weak dollar.

Table: Kenya Coffee Production Supply and Demand (PSD) - (1000 HA)(MILLION TREES)(1000 60 KG BAGS)

	2007	Revised		2008	Estimate		2009	Forecast	
	USDA Official	Post Estimate	Post Estimate New	USDA Official	Post Estimate	Post Estimate New	USDA Official	Post Estimate	Post Estimate New
Market Year Begin		10/2006	10/2006		10/2007	10/2007		10/2008	10/2008
Area Planted	167	167	167	168	168	168	0	0	170
Area Harvested	150	150	150	150	150	150	0	0	155
Bearing Trees	200	200	200	200	200	200	0	0	200
Non-Bearing Trees	0	0	0	0	0	0	0	0	0
Total Tree Population	200	200	200	200	200	200	0	0	200
Beginning Stocks	534	418	534	712	466	635	592	498	624
Arabica Production	916	916	867	798	950	667	0	0	917
Robusta Production	2	2	2	2	2	2	0	0	2
Other Production	0	0	0	0	0	0	0	0	0
Total Production	918	918	869	800	952	669	0	0	919
Bean Imports	0	0	0	0	0	0	0	0	0
Roast & Ground Imports	0	0	0	0	0	0	0	0	0
Soluble Imports	3	3	3	3	3	3	0	0	3
Total Imports	3	3	3	3	3	3	0	0	3
Total Supply	1455	1339	1406	1515	1421	1307	592	498	1546
Bean Exports	720	850	748	900	900	660	0	0	807
Rst-Grnd Exp.	0	0	0	0	0	0	0	0	0
Soluble Exports	0	0	0	0	0	0	0	0	0
Total Exports	720	850	748	900	900	660	0	0	807
Rst,Ground Dom. Consum	20	20	20	20	20	20	0	0	20
Soluble Dom. Cons.	3	3	3	3	3	3	0	0	3
Domestic Use	23	23	23	23	23	23	0	0	23
Ending Stocks	712	466	635	592	498	624	0	0	716
Total Distribution	1455	1339	1406	1515	1421	1307	0	0	1546
Exportable Production	895	895	846	777	929	646	0	0	896

The cold season that is characteristic of the months of June/July started mid May 2007 and continued into August 2007. The prolonged and intense cold weather brought a severe CBD attack that drastically reduced the crop prospects, hampering flowering. West of the Rift Valley, the cold weather was accompanied by continuous rains depressing the capacity of the coffee bushes to flower, consequently affecting the overall production. The weather conditions favored the proliferation of CBD resulting in huge late crop losses. A study by the Coffee Research Foundation on behalf of Kenya Coffee Traders Association and the World

Bank reported a crop loss of up to 80 percent in some of the traditional coffee variety dominated farms in upper zones of Embu, Kirinyaga, and Nyeri. However, some good quality coffees are expected from the high altitude areas. FAS forecasts almost 30 percent increase for MY 2008/09, as a consequence of the coffee biennial bearing cycles.

Coffee yield and crop husbandry

The diverse farm setting that characterizes the coffee production zones make it very challenging with its production costs varying with different management abilities. Small scale farmers' coffee holdings average 0.5 hectares with production typically rain fed. Yields as well as expenditure on per hectare basis are invariably higher on farms that have better husbandry and management practices. Presently average yield performance ranges from a low of about 220 kg of clean coffee (low management) to over 900 kg of clean coffee (high management in the smallholder sub sector). The estate sector has higher management and consequently higher returns.

Due to price instability and high cost of coffee production inter-cropping with corn, beans and other food and tree crops continues to be widespread, improving farm income and food supply. This has impacted negatively on both yield and quality of coffee. Coffee area is threatened as farmers from the main coffee growing region engage in more profitable agricultural enterprises mainly horticulture and dairy. This is especially true in the Mount Kenya region and Nyanza province. Emerging Interest from non-traditional coffee growing regions is likely to sustain area as the farmers shift from corn farming to coffee due to higher returns from coffee. The farmers from western Kenya have formed unique co-operatives and hand pulp their coffee to deliver to the co-operative society for marketing.

Despite its decline, the coffee sector continues to be a critical economic driver for Kenya, the country also continues to be a market leader in premium coffee sector with over 99 % of the country's production being Arabica.

Plant material demand high

Reports from the Coffee Research Foundation (CRF) indicate that planting material demand is higher than supply. The increased demand of planting material could be an indicator of both rehabilitation and replanting of formerly abandoned farms. Demand for Ruiru 11 (a hybrid) which is resistant to both CBD and Coffee Leaf Rust (CLR) is on the increase. CBD and CLR are increasingly becoming a major factor and may constrain coffee production and quality if not contained. The costs of spraying the traditional coffee varieties (fungicides (copper based)) have sky rocketed from a low of Kshs 300 to a high of Kshs 900 per kg within a one year span. This will likely jeopardize crop protection in the coming year and also increase demand for disease resistant planting materials. The capacity for production of planting materials at the Coffee Research Foundation at Ruiru has been enhanced after the completion of new Tissue Culture Laboratories.

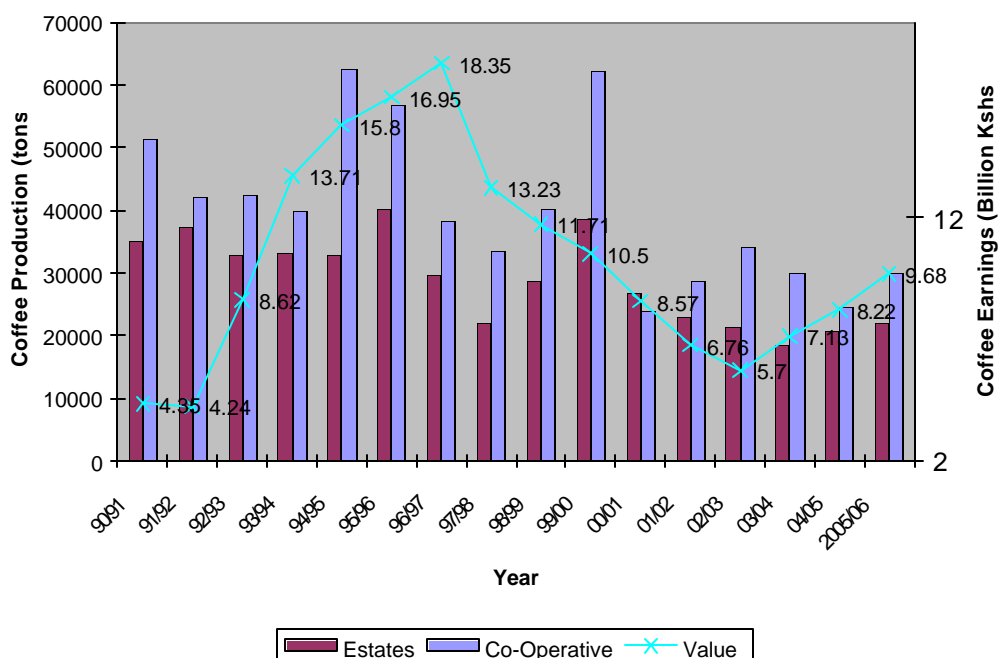
Trade

Kenya coffee exports in MY 2005/06 and 2006/07 were reported as 37,867 and 44,901 tons respectively.

Export Trade Matrix			
Country	Kenya		
Commodity	Coffee, Green		
Time Period	2005/06	Units:	2006/07
Exports for:	2006	Tons	2007
U.S.	6,189	U.S.	4,802
Others		Others	
Germany	11,343	Germany	11,439
Sweden	4,506	Sweden	7,347
Belgium	2,368	Belgium	4,753
UK	2,491	UK	2,043
Finland	2,465	Finland	3,158
Netherlands	2,019	Netherlands	2,524
Norway	869	Norway	1,191
Denmark	598	Denmark	418
Poland	678	Poland	632
Canada	547	Canada	1,307
Total for Others	27,884		34,812
Others not Listed	3,794		5,287
Grand Total	37,867		44,901

Source: Coffee Board of Kenya

Kenya Coffee Production and Earnings



Though coffee prices have frequently fallen below the cost of production in the last decade, the improved prices and earnings as indicated by the graph are likely to have positive

impacts on volume and quality. As shown on the graph estate production has taken an upward trend albeit slowly.

The country earned Kshs 8.8 billion during 2006/07 a decline from the previous year (Kshs 9.6 billion). The value decline is mainly due to the strong Kenya Shilling.

Policy & Marketing

GOK has put in place efforts to resuscitate the industry which has hit a record low. The government has written off Kshs 3.2 billion worth of debts owed by farmers and established a development fund (Kshs 600 million available to farmers in 2008) for affordable credit. Save for the estates sub-sector, crop husbandry in most of the smallholder remains below average. Coffee analysts feel access to credit facilities has been the major drawback towards the implementation of sound husbandry practices. The recently launched Coffee Development Fund (CoDF) is expected to assist the industry could address the constraint.

GOK through the Ministry of Trade and Industry is implementing a pilot value chain based matching grant fund project. The project is supplemented by the World Bank managed by Deloitte Consultancy Limited as parts of Public/Private sector partnership (PPT). The value chain based grant fund focuses on three key value chains coffee, cotton and pyrethrum.

During the second half of 2006 GOK authorized the new legislation commonly known as the 'Second Window' to run parallel with the auction system. Prior to the new legislation coffee was marketed under the central marketing system of the Nairobi Coffee Exchange. Some analysts believed that it restricted farmers to one trading system. The gazetted rules define the second window as a contractual agreement between the growers and the marketing agent and a buyer located outside Kenya for the sale of clean coffee. The marketing agent must demonstrate ability to access overseas market, conduct market research and provide a bank guarantee to protect farmers' money.

Coffee exports using the 'second window' are still minimal with many seeing it as an opportunity but with risks. Industry analysts argue that the second window needed to have been more liberalized; presently the farmer is required to operate through a marketing agent who must be approved by the GOK. The involvement of coffee dealers as marketing agents has also been questioned with industry participants seeing a possible undermining of prices at the auction. The estate farmers and the large co-operatives are the likely beneficiaries of the second window.